

## Message Text

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ACTION EUR-12

INFO OCT-01 EA-07 IO-13 ISO-00 SP-02 AID-05 EB-07 NSC-05

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FRB-03 INR-07 NSAE-00 XMB-02 OPIC-03 LAB-04 SIL-01

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FM AMEMBASSY ROME

TO SECSTATE WASH DC IMMEDIATE 9277

TREASURY DEPARTMENT WASH DC IMMEDIATE

INFO AMEMBASSY BERN

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TREASURY FOR SYVRUD

PASS FRB

E.O. 11652: N/A

TAGS: EFIN, IT

SUBJECT: ECONOMIC PORTION OF ANDREOTTI PROGRAM

REF: (A) ROME 11956, (B) ROME 12292 (NOTAL)

SUMMARY. ADDRESS DELIVERED BY PRIME MINISTER ANDREOTTI BEFORE SENATE AND CHAMBER OF DEPUTIES AUGUST 4 CLOSELY FOLLOWED DRAFT PROGRAM REPORTED REF A. HOWEVER, ANDREOTTI WAS SOMEWHAT MORE PRECISE AS TO CONTENT AND ASSIGNED DEADLINES FOR ACTION FOR SOME PROPOSALS. THERE ARE FEW NEW PROPOSALS COMPARED TO DRAFT PROGRAM, ALTHOUGH SOME OF ORIGINAL IDEAS HAVE BEEN MODIFIED AND OTHER OMITTED. (OMISSION OF ITEM NEED NOT NECESSARILY MEAN THAT PARTICULAR IDEA HAS BEEN COMPLETELY ABANDONED.) MODIFIED PROGRAM IN ECONOMIC STABILIZATION AREAS IS SOMEWHAT IMPROVED OVER DRAFT PROGRAM BUT IS STILL TOO VAGUE TO SERVE AS QUID PRO QUO FOR NEW FOREIGN FINANCING. FURTHER DEVELOPMENT OF DETAILS OF PROGRAM COULD MERIT CONSIDERATION BY ABOUT OCTOBER OR NOVEMBER. END SUMMARY.

1. PRIME MINISTER ANDREOTTI DELIVERED 80-PAGE ADDRESS FIRST TO SENATE AND THEN TO CHAMBER OF DEPUTIES ON AUGUST 4. ADDRESS WAS RATHER HEAVILY CONCENTRATED ON ECONOMIC MATTERS AND FOLLOWED QUITE CLOSELY TEXT OF DRAFT PROGRAM WHICH HAD BEEN CIRCULATED AMONG POLITICAL PARTIES (REF A). FOLLOWING REPORT CONCENTRATES MAINLY ON ECONOMIC STABILIZATION ASPECTS OF ANDREOTTI PROGRAM, HIGHLIGHTING DIFFERENCES BETWEEN CURRENT PROGRAM AND EARLIER DRAFT VERSION. EXCEPT FOR COMMITMENT TO PRESENT BY END-SEPTEMBER NEW DRAFT LAW FOR CREATION OF INDUSTRIAL RECONVERSION FUND AND DECREE CONCERNING ENERGY CONSERVATION THERE WERE FEW CHANGES IN SECTORAL ASPECTS OF DRAFT PROGRAM (E.G., INDUSTRY, AGRICULTURE, MEZZOGIORNO, HOUSING, TRANSPORT, ENERGY, ETC.).

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2. ECONOMIC SITUATION. ANDREOTTI DESCRIBES BOTH POSITIVE AND NEGATIVE ASPECTS OF ITALY'S CURRENT ECONOMIC SITUATION. POSITIVE ASPECTS ARE: (A) ECONOMIC RECOVERY IN ITALY, (B) AND IMPROVED INTERNATIONAL ECONOMIC SITUATION, (C) GREATER STABILITY OF LIRA, AND (D) SOME RETURN OF CONFIDENCE. NEGATIVE FACTORS ARE: (A) CONTINUED NEED FOR TIGHT CREDIT WHICH MAY EVENTUALLY THREATEN RECOVERY, (B) INSTABILITY IN INTERNATIONAL EXCHANGE MARKETS, AND (C)

DIFFICULTY IN OBTAINING ADEQUATE COOPERATION OF SOCIAL FORCES IN FIGHT AGAINST INFLATION. ANDREOTTI IDENTIFIES CRITICAL FACTORS SHAPING ITALY'S ECONOMIC POLICY AS ITS LARGE FOREIGN DEBT, CONTINUED BALANCE OF PAYMENTS DEFICITS, PRICE INFLATION AND LARGE BUDGET DEFICIT. CHIEF POLICY AIMS OF GOVERNMENT WILL BE TO REDUCE INFLATION, TO CONTAIN BALANCE OF PAYMENTS DEFICIT, TO DEFEND LIRA EXCHANGE RATE, TO IMPROVE EFFICIENCY OF ITALIAN ECONOMY AND TO EXPAND PRODUCTION AND EMPLOYMENT. TO ACHIEVE THESE GOALS, THERE MUST BE AN IMPROVED ECONOMIC/SOCIAL CLIMATE; BOTH PUBLIC AND PRIVATE ENTERPRISE MUST BECOME MORE EFFICIENT; PRODUCTION COSTS MUST BE REDUCED AND PROFIT MARGINS RESTORED; AND THERE MUST BE A BETTER ALLOCATION OF RESOURCES OF THE PUBLIC SECTOR. IN ADDITION, ITALY'S INVESTMENT TO GDP RATIO MUST BE INCREASED, WITH HIGH INVESTMENT PRIORITIES ASSIGNED TO IMPORT SUBSTITUTION AND EXPORT GROWTH. PRIVATE CONSUMPTION MUST DECLINE RELATIVE TO THAT OF INVESTMENT AND EXPORTS.

3. REFORM OF ECONOMIC PLANNING STRUCTURE. ANDREOTTI PROGRAM CALLS FOR REORGANIZATION OF MINISTRY OF BUDGET AND PLANNING AND MINISTRY OF FOREIGN TRADE, AS WELL AS RESTRUCTURING GOVERNMENT STATISTICAL AND ECONOMIC RESEARCH INSTITUTES (ISTAT, ISCO AND ISPE). IT SUGGESTS THAT SUBCOMMITTEE OF THE COMMITTEE FOR THE ECONOMY AND LABOR (CNEL) MIGHT BE ASSIGNED RESPONSIBILITY FOR SUPERVISING IMPLEMENTATION OF ECONOMIC AND SOCIAL PROGRAMS ADOPTED BY THE GOVERNMENT AND BY PARLIAMENT. IN ADDITION, GOVERNMENT PROPOSES TO SUBMIT DRAFT LAW TO PARLIAMENT TO SIMPLIFY SYSTEM OF AUDITING OF PUBLIC MONIES SO AS TO REDUCE REQUIREMENT FOR PRE-AUDITS TO THOSE ACTIONS OF PARTICULAR IMPORTANCE, EITHER BECAUSE OF THE SUBJECT INVOLVED OR THE AMOUNT OF PUBLIC FUNDS INVOLVED. MAIN BURDEN OF CONTROL LIMITED OFFICIAL USE

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ON USE OF PUBLIC MONIES WOULD THEN FALL UPON POST AUDITS, SUPPORTED BY ADEQUATE SANCTIONS.

4. PUBLIC FINANCE. THE FOLLOWING ARE MAIN ADDITIONS OR MODIFICATIONS TO PUBLIC FINANCE PROPOSALS CONTAINED IN DRAFT PROGRAM (PARA 5.A. TO 5.E. OF REF A).

(A) THE PROPOSED TWO-THIRDS REDUCTION IN RATIO OF 1975 BUDGET DEFICIT TO GDP (BY 1979) IS DEFINED AS APPLICABLE TO CASH BUDGET DEFICIT IN FORM OF TOTAL FINANCIAL NEEDS OF TREASURY. THIS APPEARS TO BE REFERENCE TO CASH BUDGET DEFICIT CONCEPT USED BY IMF AND EC IN ESTABLISHING LOAN CONDITIONS, RATHER THAN TO DEFICIT OF ENTIRE PUBLIC SECTOR WHICH WAS REFERRED TO IN DRAFT PROGRAM. USING THIS MEASURE, 1977 BUDGET ESTIMATES AND ASSUMPTIONS SIMILAR TO THOSE CONTAINED IN PARA 1 REF B, PATTERN OF REDUCTION IN RATIO OF

THIS DEFICIT TO GDP MIGHT BE APPROXIMATELY AS FOLLOWS (SEE  
TABLE LA OF REF B):

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TREASURY CASH DEFICIT/GDP RATIO  
(BILLIONS OF LIRE: PERCENT)

1975

DEFICIT 14,170

GDP 112,358

PERCENT 12.6

1976E

DEFICIT1) 13,800

GDP 136,000

034:3,5 10.1

1977 13,600E

GDP165,000

PERCENT 8.2

1978

DEFICIT1) 10,210

GDP 185,600

PERCENT 5.5

1979

DEFICIT 8,575

GDP 204,160

PERCENT 4.2

E-ESTIMATE

1) BOI/IMF/EC DEFINITION

SOURCE: 1975 BANK OF ITALY REPORT

(B) AS IMMEDIATE MEASURE TO REDUCE EXPENDITURES  
ANDREOTTI COMMITS GOI TO PRESENT CONCRETE PROPOSALS FOR  
LIMITING NEW EXPENDITURES AND FOR CANCELLING SOME OLD  
APPROPRIATIONS IN TIME FOR PARLIAMENTARY COMMITTEES' DEBATE  
ON 1977 BUDGET (I.E., AROUND OCTOBER 1976).

(C) SPECIAL COMMITTEE OF EXPERTS IS TO MAKE CONCRETE  
PROPOSALS FOR DEALING WITH "RESIDUI PASSIVI," (ACCIMILATION  
OF APPROPRIATED BUT UNSPENT FUNDS).

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(D) IN ADDITION TO TAX EVASION PROPOSALS CONTAINED IN DRAFT PROGRAM (E.G., SELECTIVE AUDITS), GOI WILL SUBMIT FURTHER SUGGESTIONS TO PARLIAMENT WITHIN FOUR MONTHS.

(E) WITHIN FIRST TEN DAYS OF SEPTEMBER GOVERNMENT WILL SUBMIT TO PARLIAMENT LEGISLATIVE MEASURE TO REPLACE REVENUE LOST AS RESULT OF RECENT DECISION BY CONSTITUTIONAL COURT THAT JOINT INCOME TAX RETURNS (CUMULO DEI REDDITI) ARE UNCONSTITUTIONAL. (PREVIOUS GOVERNMENT TEMPORARILY SUSPENDED TAX COLLECTIONS ON JOINT RETURNS OF MARRIED COUPLES. REVENUE LOSS IS ESTIMATED AT ABOUT 600 BILLION LIRE. UNSPECIFIED SEPTEMBER TAX MEASURE US AIMED AT RESTORING COLLECTION OF TAXES ON THOSE EARLIER EXCLUDED.)

(F) BY MID-OCTOBER GOI WILL SUBMIT LAW TO CREATE "EQUITABLE" SYSTEM OF TAXATION OF INCOME OF MARRIED COUPLES CONSISTENT WITH DECISION BY CONSTITUTIONAL COURT. IN THIS CONNECTION, REVISION OF PERSONAL INCOME TAX PROGRESSIVELY TO ACHIEVE AVERAGE EUROPEAN LEVEL IS OMITTED.)

(G) INCREASE IN PUBLIC SERVICE TARIFFS MUST NOT HAVE EFFECT OF FEEDING INFLATION THROUGH WAGE INDEXATION SYSTEM.

(H) LIMITATION ON WAGE AND SALARY INCREASES OF DEPENDENT LABOR WHICH IN DRAFT PROGRAM REFERRED GENERALLY TO HIGH INCOME LEVELS NOW HAS BEEN CHANGED SO THAT WAGE INDEXATION ADJUSTMENTS WOULD BE APPLIED IN HIGHLY PROGRESSIVE MANNER AND AT UNSPECIFIED HIGH LEVEL OF SALARIES (AMOUNT TO BE AGREED UPON), ALL TYPES OF INCREASES WOULD BE TEMPORARILY BLOCKED. PROGRAM DOES NOT REPEAT IDEA IN DRAFT PROGRAM OF EARMARKING THESE LABOR COST SAVINGS FOR PRODUCTIVE INVESTMENT.

(I) PROPOSED CONSOLIDATION OF LOCAL GOVERNMENT DEBT IS LINKED TO DECEMBER 31, 1977 TERMINATION DATE OF TRANSITIONAL REVENUE-SHARING PROCEDURES ESTABLISHED IN 1971 TAX REFORM BASIC LAW.

(J) REFERENCE TO POSSIBLE RESTORATION OF AUTONOMOUS TAX AUTHORITY TO LOCAL GOVERNMENTS HAS BEEN SOMEWHAT WEAKENED BY SPECIFYING THAT ANY SUCH MEASURE SHOULD NOT REOPEN LIMITED OFFICIAL USE

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BASIC TAX REFORM SYSTEM CREATED IN 1971 LAW.

(K) PROGRAM SUGGESTS THAT NEED FOR CONTINUED EXISTENCE OF PROVINCIAL GOVERNMENTS SHOULD BE FURTHER EXAMINED.

5. FOLLOWING PROPOSALS WHICH APPEARED IN DRAFT PROGRAM HAVE

BEEN OMITTED FROM FINAL VERSION:

(A) REFERENCE TO INCREASING TAX BASE SPECIFICALLY ON  
INCOME FROM CAPITAL GAINS AND REAL ESTATE, ALTHOUGH GENERAL  
REFERENCE TO INCREASING TAX BASE REMAINS.

(B) REDUCTION IN TAX BENEFITS AND CHANNELING TO LOCAL  
GOVERNMENTS OF CORRESPONDING INCREASE IN REVENUE.

(C) COOPERATION OF LOCAL AUTHORITIES IN TAX ASSESSMENT.

(D) CREATION OF NEW BODY TO DETERMINE AMOUNTS AND  
PURPOSES OF TRANSFER PAYMENTS FROM CENTRAL GOVERNMENT TO  
LOCAL GOVERNMENTS.

(E) CONCENTRATION OF CREDITS TO LOCAL GOVERNMENTS THROUGH  
SINGLE FINANCIAL INSTITUTION.

(F) THREE-YEAR FREEZE ON HIRING AT LOCAL GOVERNMENT LEVEL.

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AMCONSUL NAPLES  
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6. SOCIAL POLICY. ONLY INNOVATIONS IN THIS AREA COMPARED TO DRAFT PROGRAM ARE: (A) PROPOSED SERIOUS EXAMINATION WITH BUSINESS AND LABOR OF WAGE INDEXATION, WAGE SUPPLEMENT AND UNEMPLOYMENT INSURANCE PROGRAMS IS TO TAKE PLACE "AS SOON AS POSSIBLE;" AND (B) DRAFT LAW ON EMPLOYMENT OF YOUTH IS TO BE SUBMITTED TO PARLIAMENT IN OCTOBER.

7. BALANCE OF PAYMENTS. FOLLOWING ARE ITEMS WHICH ARE EITHER NEW OR MORE DETAILED THAN THOSE IN DRAFT PROGRAM:

(A) POSSIBILITY IS TO BE FURTHER EXAMINED OF RE-INTRODUCING SYSTEM OF IMPORTS "FRANCO VALUTO" (I.E., WITH PAYMENTS MADE FROM FOREIGN EXCHANGE SOURCES OUTSIDE ITALY) AS MENTIONED OF ENCOURAGING USE OF ILLEGALLY EXPORTED CAPITAL.

(B) SUBJECT TO FURTHER STUDY, THERE COULD BE SPECIAL DOLLAR LOAN ISSUE TO BE SUBSCRIBED IN FOREIGN CURRENCY BUT REDEEMABLE IN LIRE, POSSIBLY LINKED TO EARLY REPATRIATION OF PROCEEDS FROM EXPORTS SOLD ON CREDIT AND TO EXTENSION UNTIL END YEAR OF PERIOD FOR REPATRIATING ILLEGALLY EXPORTED CAPITAL UNDER RECENT FOREIGN EXCHANGE CONTROL AMNESTY.

(C) GOI NEGOTIATION OF IMF STANDBY IS TO BE RESUMED



IN SEPTEMBER, ALONG WITH REQUEST FOR EXTENSION OF \$2  
BILLION GOLD COLLATERAL LOAN WITH BUDESBANK.

8. COMMENT. INITIAL PRESS REACTION TO ANDREOTTI PROGRAM  
HAS BEEN SOMEWHAT CRITICAL ON GROUNDS THAT PROGRAM IS STILL  
TOO COMPREHENSIVE AND TOO VAGUE. HOWEVER, CREDIT IS GIVEN  
FOR INCLUSION OF SPECIFIC TIMING DEADLINES FOR SUBMISSION  
OF CERTAIN PARTS OF PROGRAM TO PARLIAMENT.

9. SOME IMPROVEMENTS IN ANDREOTTI PROGRAM COMPARED TO  
ORIGINAL DRAFT INCLUDE: (A) SPECIFIC EFFORT TO REDUCE  
EXPENDITURES IN 1977 BUDGET AND TO EXAMINE BACKLOG OF FUNDS  
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APPROPRIATED BUT NOT YET SPENT, (B) FIXING OF SEPTEMBER  
DEADLINE FOR REPLACING REVENUE LOST AS RESULT OF UNCONSTITU-  
TIONALITY OF JOINT INCOME TAX RETURNS, (C) ESTABLISHMENT OF  
MID-OCTOBER DEADLINE FOR REGULATING TAXATION OF INCOME OF  
MARRIED COUPLES WITH POSSIBLE INCLUSION OF TAX RATE INCREASES  
ON PERSONAL INCOME, (D) PROPOSAL THAT PUBLIC TARIFF RATE  
INCREASES NOT BE ALLOWED TO GENERATE INFLATION THROUGH WAGE  
INDEXATION SYSTEM (I.E., ACCEPTANCE OF IDEA FLOATED BY BOI  
GOVERNOR BAFFI IN MAY), AND (E) IDEA OF PROGRESSIVE REDUCTION  
OF COST-OF-LIVING WAGE ADJUSTMENT TO MEDIUM AND HIGH LEVEL  
WAGE AND SALARY EARNERS AS WELL AS FULL BLOCK OF INCREASES  
AT TO-BE-NEGOTIATED HIGHER SALARY LEVEL. (ANDREOTTI DID NOT  
ACCEPT AN 8 MILLION LIRE CUT-OFF PROPOSED BY UNIONS, WHICH  
WOULD HAVE LITTLE MORE THAN SYMBOLIC EFFECT ON TOTAL  
WAGE BILL.)

10. SOME AREAS WHERE ANDREOTTI PROGRAM IS LESS RIGOROUS  
THAN DRAFT VERSION INCLUDE: (A) APPARENT PARTIAL RETREAT  
ON QUESTION OF LOCAL TAX AUTONOMY ON GROUNDS THAT ORIGINAL  
REVENUE SHARING CONCEPT EMBODIED IN TAX REFORM LAW SHOULD BE  
PRESERVED, (IF GROWTH OF LOCAL GOVERNMENT EXPENDITURES CAN  
BE LIMITED AND CENTRAL GOVERNMENT'S CAPACITY TO GENERATE  
REVENUE INCREASED THIS NEED NOT BE SERIOUS LACK (B) ABSENCE  
OF SUGGESTION FOR THREE-YEAR FREEZE ON HIRING OF LOCAL  
GOVERNMENT EMPLOYEES WHICH COULD BE RATHER SERIOUS GAP IN  
PROGRAM TO LIMIT DEFICITS OF LOCAL GOVERNMENTS. SOME OF  
THE ITEMS REFERRED TO IN DRAFT PROGRAM WHICH ARE MISSING  
IN FINAL VERSION (E.G. COOPERATION OF LOCAL TAX AUTHORITIES  
IN TAX ASSESSMENT AND CREATION OF NEW BODY TO CONTROL  
GOVERNMENT EXPENDITURES) TO SOME EXTENT ALREADY EXIST OR  
WERE CALLED FOR IN ORIGINAL 1971 TAX REFORM ENABLING LAW.

1. ON BALANCE, EMBASSY BELIEVES THAT ANDREOTTI PROGRAM  
IN FINAL VERSION IS IMPROVEMENT OVER ORIGINAL DRAFT, BOTH  
IN ITS DEGREE OF SPECIFICITY AND IN THE ESTABLISHMENT OF  
TARGET DEADLINES FOR INTRODUCING SOME MEASURES. PROGRAM

IS STILL TOO GENERAL TO MERIT SERIOUS CONSIDERATION BY  
FOREIGN LENDERS AS QUID PRO QUO FOR NEW FOREIGN FINANCING.  
HOWEVER, DETAILS OF PROPOSALS, PARTICULARLY REGARDING  
BUDGET DEFICIT AND LABOR COST FIELDS, MAY BE SUFFICIENTLY  
DEVELOPED FOLLOWING PRESENTATION OF SPECIFIC LEGISLATIVE  
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PROPOSALS TO PARLIAMENT AND NEGOTIATIONS WITH LABOR AND  
BUSINESS AS TO MERIT CONSIDERATION BY FOREIGN LENDERS AS  
SOON AS OCTOBER OR NOVEMBER 1976. VOLPE

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**Draft Date:** 05 AUG 1976  
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**Decaption Note:**  
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**Disposition Approved on Date:**  
**Disposition Authority:** BoyleJA  
**Disposition Case Number:** n/a  
**Disposition Comment:** 25 YEAR REVIEW  
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**Disposition Event:**  
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